

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

RECEIVED
MAY - 7 1996
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

In the Matter of

)

)

Federal-State Joint Board on
Universal Service

)

)

CC Docket No. 96-45

REPLY

DOCKET FILE COPY ORIGINAL

National Exchange Carrier Association, Inc.
100 South Jefferson Road
Whippany, New Jersey 07981

May 7, 1996

054

TABLE OF CONTENTS

SUMMARY	ii
I. THE RECORD SHOWS THAT STRONG FEDERAL POLICIES AND PROGRAMS ARE NEEDED TO PRESERVE AND ADVANCE UNIVERSAL SERVICE	3
II. THE COMMISSION SHOULD REPLACE THE CURRENT TARIFF-BASED UNIVERSAL SERVICE COLLECTION MECHANISM WITH A REVENUE-BASED CONTRIBUTION SYSTEM	14
III. THE COMMISSION SHOULD APPOINT NECA AS ADMINISTRATOR OF THE NEW UNIVERSAL SERVICE FUND.	17
IV. CONCLUSION	24
APPENDIX A: List of Commenters and Abbreviations	A-1

SUMMARY

The record in this proceeding, as well as that assembled in CC Docket No. 80-286, shows that strong federal policies and programs are needed to preserve and advance universal service. Commenters from across the spectrum agree that universal service is a critical issue, and that efforts to nurture competition must not undermine existing universal service achievements or slow the expansion of modern services to areas that remain unserved or underserved.

The Joint Board and the Commission must act soon to propose specific rules in this proceeding, so that interested persons have a meaningful opportunity to comment. By moving forward with specific proposals, the Joint Board and Commission will reduce uncertainty, which in itself can be harmful to universal service expansion plans.

Based on the record, NECA believes that the Commission should, at a minimum, propose rules that (a) build on existing cost-based universal service mechanisms, including the Universal Service Fund (USF) and Dial Equipment Minutes (DEM) weighting, while allowing exchange carriers to experiment with new costing methodologies such as proxies; (b) change the current PSL-based tariff methodology for collecting universal service support amounts to a revenue-based system with payments required by rule; and (c) use existing lifeline assistance programs as a model for funding for discounts on services provided to schools, libraries and rural health care providers.

In addition, the record in this proceeding supports the continuation of NECA as administrator of federal universal service support programs. Numerous parties, including a significant number of state public utility commissions, LEC consultants, and state telephone associations, describe the value of NECA's expertise and the scope of NECA's in-place resources. These commenters recognize NECA's capabilities in administering current universal service programs in a fair,

competitively-neutral and cost-effective manner. The Commission should continue to rely on NECA as administrator of federal universal service support mechanisms, rather than delegate these functions to separate state administrations or start over with a new entity.

These steps will put the Joint Board and the Commission on a path that will ensure compliance with the universal service goals of the 1996 Act, and enable the Commission to focus its resources on the many other critical issues (including access reform) presented by the 1996 Act and

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)	
)	
Federal-State Joint Board on)	CC Docket No. 96-45
Universal Service)	

REPLY

The record in this proceeding overwhelmingly supports the need for strong federal universal service programs and policies. Over 240 interested persons filed comments in response to the Commission's NPRM.¹ Nearly all emphasize that universal service, now an explicit part of the Communications Act under new section 254, should be treated as a vital part of telecommunications policy. The Wyoming PSC states, and NECA agrees, that "[a]mong the issues presented in the federal Telecommunications Act of 1996 . . . none is more important than universal service."² Century and TDS, in their joint comments, also emphasize the strength of the 1996 Act's commitment to universal service:

The new law has carefully balanced its expanded national commitment to competition and decreasing regulation . . . and its expanded national commitment to the 'preservation and advancement of universal service' . . . The resulting new federal

¹ Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Notice of Proposed Rulemaking and Order Establishing Joint Board, 61 Fed. Reg. 10499 (March 14, 1996), FCC 96-93 (rel. March 8, 1996) (NPRM). On April 1, 1996, Commission extended deadline for filing comments in this proceeding to April 12, 1996. Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Order, 61 Fed. Reg. 15208 (April 5, 1996), DA 96-483 (rel. April 1, 1996). An alphabetical list of entities filing NPRM Comments is attached as Appendix A. Abbreviations used in this Reply are set forth in Appendix A.

² Wyoming PSC at 1. See also NCTA at ii and 2 ("Basic telephone service is an essential service; "affordable telephone service in rural, insular, and high cost areas must remain a high priority . . .").

universal service ‘principles’ embody a national commitment to ‘quality’ services at ‘just, reasonable and affordable’ rates, nationwide access to evolving advanced telecommunications capabilities and information services, and ‘reasonably comparable’ urban and rural services and rates.³

The comments in this proceeding reflect a broad diversity of views, extending to topics far beyond those encompassed by CC Docket No. 80-286. It will be difficult to reconcile the conflicting views presented in the short time allowed under the Act. Nevertheless, the Joint Board and Commission must act soon to propose specific rules in this proceeding if the time frame provided for under section 254(a) of the Act is to be met.⁴ Continued uncertainty in this area is harmful to universal service. Telephone companies who would otherwise be moving forward with plans for service upgrades and expansions, understandably, are reluctant to commit resources and investments in infrastructure until cost recovery issues are clarified.

Based on the record assembled so far in this proceeding and in CC Docket No. 80-286,⁵ NECA recommends, at a minimum, that the Commission propose rules that (a) build on existing cost-based universal service mechanisms, including the Universal Service Fund (USF) and Dial Equipment

³ Century and TDS (joint comments) at 2.

⁴ A number of commenters point out that specific proposed rules are necessary in order to allow interested persons a meaningful opportunity to comment. See, e.g., Missouri PSC (MoPSC) at 3-4 (another NPRM is needed -- “the present NPRM has the form of a Notice of Inquiry . . . it does not propose a specific rule. As a result the NPRM deprives the commentators of meaningful notice of what is being proposed . . . The 1996 Act also permits the FCC to engage in such other proceedings as necessary . . . MoPSC looks forward to commenting on an actual proposed rule in such proceedings.”); RTC at l. n. 1 and 19-20.

⁵ Amendment of Part 36 of the Commission’s Rules And Establishment of a Joint Board, Notice of Inquiry, 9 FCC Rcd 7404 (1994) (1994 NOI), comments filed October 28, 1994 (1994 NOI Comments), replies filed December 2, 1994 (1994 NOI Replies); Amendment of Part 36 of the Commission’s Rules And Establishment of a Joint Board, Notice of Proposed Rulemaking and Notice of Inquiry, 10 FCC Rcd 12309 (1995) (1995 NPRM), comments filed on October 10, 1995 (1995 NPRM Comments), replies filed November 9, 1995 (1995 NPRM Replies).

Minutes (DEM) weighting, while allowing exchange carriers to experiment with new costing methodologies such as proxies; (b) change the current PSL-based tariff methodology for collecting universal service support amounts to a revenue-based system with payments required by rule; (c) use the existing lifeline assistance programs as a model for funding for discounts on services provided to schools, libraries and rural health care providers; and (d) continue NECA as administrator of federal universal support programs. These steps will put the Joint Board and the Commission on a path that will ensure compliance with the universal service goals of the 1996 Act, and enable the Commission to focus its resources on the many other critical issues (including access reform) presented by the 1996 Act and industry changes.

I. THE RECORD SHOWS THAT STRONG FEDERAL POLICIES AND PROGRAMS ARE NEEDED TO PRESERVE AND ADVANCE UNIVERSAL SERVICE.

With universal service now established as an explicit goal in new section 254(b) of the Communications Act,⁶ almost all commenters in this proceeding agree that strong federal policies and programs are needed to preserve and advance universal service. Joint comments filed by the public utilities commissions of Maine, Montana, Nebraska, New Hampshire, New Mexico, Utah, Vermont

⁶ The statutory goals include (1) the availability of quality services at just, reasonable and affordable rates; (2) access to advanced telecommunications and information services in all regions; (3) that consumers in all regions, including low-income consumers and those in rural, insular, and high-cost areas, should have access to telecommunications and information services (including interexchange services and advanced telecommunications and information services) that are reasonably comparable in quality and price to those in urban areas; (4) that all providers of telecommunications services should make equitable and nondiscriminatory contributions to the preservation and advancement of universal service; (5) that there should be specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service; (6) that elementary and secondary schools and classrooms, health care providers and libraries should have access to advanced telecommunications services; and (7) such other principles as the Joint Board and Commission determine are necessary and appropriate for the protection of the public interest, convenience and necessity and that are consistent with the 1996 Act. 47 U.S.C. § 254(b)(1) - (7).

and West Virginia, for example, clearly state that the achievement of reasonably comparable rates is a federal responsibility and that state programs to support universal service are supplementary to the federal effort.⁷

NECA agrees that revisions to federal universal service programs made in response to the 1996 Act should build on the success of existing mechanisms. In particular, the continued availability of cost-based funding, including amounts determined pursuant to the Commission's USF and DEM weighting rules, is critical to the maintenance of current universal service achievements.⁸ These programs have helped telephone companies extend service to consumers in many areas of the country who would not otherwise be able to afford service.⁹ As the Montana PSC (in a separate statement) states, "[t]he FCC's Universal Service programs have effectively promoted the development of

⁷ Joint Comments of the Maine PUC, *et. al.* at 14 ("the principal responsibility for raising funds and distributing funds lies with the Commission").

⁸ See, e.g., Cheyenne Sioux River Telephone Authority and Golden West Telecom. Coop at 5 ("any changes made to universal service support mechanisms must not jeopardize existing levels of service and the provision of new service to unserved areas."); Wyoming PSC at 17-18 (suggesting that the DEM weighting cost recovery program be continued during any period of transition set by the Commission while new support mechanisms are being put into place under the Act and that weighted DEM should be considered an "appropriate permanent companion to a new federal universal service fund"); Park Region at 3 (loss of "the support of small company cost recovery mechanisms such as DEM weighting . . . would severely impair [its] ability to invest in the future infrastructure stressed in the . . . Act.").

⁹ See Minn. Tel. Assoc. at 1 ("present system has worked well in helping meet the public needs . . . local service competition and a new competitive environment necessitate making some adjustments. Current universal service funding mechanisms are a success story . . . it is best to build on the strengths of the current programs rather than reinventing a new complex system . . . any attempts to significantly alter present programs [should] be carefully crafted."). See also Joint Comments of People for the American Way, *et. al.* at iii ("Congress made plain that the universal service provisions of the 1996 Telecommunications Act do not replace traditional universal service principles . . . every provision of the 1996 Act builds upon these principles to broaden the types of services included and recipients covered . . .").

telecommunications infrastructure in high cost areas while keeping local rates affordable . . . these or similar programs must remain in place if adequate and affordable local service and present subscribership levels are to remain constant or increase in the future.”¹⁰

The job is not yet done, however. Customers in some rural and high-cost areas remain unserved, and basic service in some areas is provided using equipment that is in need of updating or replacement. Telephone companies are making progress in addressing these needs.¹¹ Reductions to current programs are likely to reverse this progress and compromise the universal service goals and principles established by the 1996 Act. NECA agrees with BellSouth: the Commission must assure that “the new mechanism will initially provide the same level of interstate support as the existing support mechanisms” and should not shift current federal support back on to the states.¹² Satisfying

¹⁰ Montana PSC at 2. See also Century and TDS at 3 (“[t]he Act’s universal service commitments are designed to overcome the economic limitations of rural markets, using a federal high cost funding mechanism to achieve section 254’s universal service purposes, bolstered by state universal service mechanisms to implement whatever additional discretionary universal service requirements a state adopts”).

¹¹ See, e.g., NECA 1995 NPRM Comments at 6-10.

¹² BellSouth at 9. Similar views were expressed by many commenters. See, e.g., Pennsylvania PUC at 2 (“[l]oss of assistance through interstate funding mechanisms may transfer more of the cost recovery burden to intrastate rates and mechanisms.”); State of Alaska at 4 (Comments filed by Attorneys for the State expressed concern that any changes made to the universal service programs should not lead to increases in telephone service rates for universal telecommunications services; rates in rural and high-cost areas must be maintained at current levels for all residents); United Utilities at 3 (the Commission should not “make any changes to its high cost and universal service programs that would shift costs and obligations onto states in a way that would undermine the goal of universal service . . . carriers will not be able to provide universal service in Alaska if the Commission shifts what are now costs funded from interstate revenue sources onto state ratepayers.”); Fort Mojave Telecom. at 2 and 5 (local residential rate is currently \$15 per month -- an affordable rate for its subscribers; company can provide this affordable rate, in part, “because of the existing Universal Service support mechanisms;” without USF revenue, customers would have estimated monthly increase in local service rate of \$143 - “[t]his reflects the importance of continuing Universal Service Principles”).

the objectives of the 1996 Act requires at least the same level of resources currently devoted to universal service, with the recognition that more may be needed as new universal service programs required by the 1996 Act are implemented.¹³

The great weight of evidence presented in CC Docket No. 80-286, incorporated within the record of this proceeding, showed that the substantial reductions proposed to current programs would be harmful to universal service.¹⁴ Comments filed in this proceeding, quoted above, amply reinforce this point. In contrast, the “minimal” and “narrow” approaches to universal service advocated by some commenters would, if adopted, be harmful to universal service and would

¹³ See, e.g., Oklahoma Corp. Comm. at 7-9 (“[a]ny reduction in current federal funding levels could dramatically thwart the achievement of the Act’s goals and objectives . . . [w]hatever mechanism is established should insure that the current level of support will not be reduced or, if it is, that adequate funding from any new mechanism will supply no less than the current level of support.”); PRTC at 2 (“[i]rrespective of the universal service support distribution methodology adopted by the Commission . . . the Commission [should] ensure that LECs serving areas with unusually low telephone penetration levels continue to receive universal service assistance at least comparable to today’s assistance until they achieve reasonable penetration levels.”)

¹⁴ In particular, program changes proposed in CC Docket No. 80-286 (elimination of DEM weighting, mandatory consolidation of affiliated study areas, removal of administrative expenses from support amounts, increases in eligibility thresholds, etc.) would be harmful to universal service. See NECA at 11-12 citing Colorado PUC 1995 NPRM Reply at 16; Alabama PSC 1995 NPRM Reply at 2. See also United States SBA at 4 (principles in Act tend to expand the definition of universal service; “[i]n this sense, they reverse the Commission’s stated goal of reducing the universal service fund which was the principal thrust of the Commission’s efforts in its previous docket on universal service.”). There is also no basis for continuing to cap universal service funding on an overall basis or to impose ad hoc individual caps on funding. See Maine PUC, et. al. at 3 (Commission “must resist the temptation to set an arbitrary limit on the funding that will be needed to achieve the statutory purpose . . . all funds needed to meet the statutory objectives must be raised and distributed.”); RTC at 6 (“Act expressly requires ‘sufficient, specific and predictable’ federal support to meet the Act’s universal service goals . . . It is thus not lawful or possible to cap total support . . .”).

frustrate the basic intent of the 1996 Act.¹⁵

A number of commenters propose supplementing existing mechanisms with non-jurisdictional methodologies that would provide support to carriers by comparing their costs (as determined by studies, proxies or some other means) with federally-determined “affordability benchmarks.” USTA, for example, proposes that the Joint Board and Commission establish an affordability benchmark set at the nationwide average interstate loop cost with support provided to the extent that interstate costs of eligible carriers (as determined by a study of incumbent LEC costs) are above the benchmark.¹⁶ USTA recognizes, however, that existing USF and DEM mechanisms must be left in place for incumbent rural telephone companies.¹⁷

AT&T proposes to base a nationwide “affordable rate” on a weighted average of Tier 1 LEC local rates, with support available to the extent that the “total service long-run incremental cost”

¹⁵ See, e.g., Frontier at 3-8, AT&T at 3-6 and 11-14, LCI at 2-3. Commenters advocating narrow approaches to universal service complain about “burdens” imposed by support mechanisms, but ignore the convincing evidence provided in CC Docket No. 80-286 showing that existing universal service achievements have come at a reasonable price. NECA demonstrated that current interstate Universal Service Fund costs are small in relation to telecommunications industry revenues. See NECA 1994 NOI Comments at 23-25; NECA 1995 NPRM Comments at 19-22. NECA also referenced data showing that USF costs represent only a small portion of total loop revenue requirements, and that the proportion of USF costs to total investment has been steadily declining since the fund’s inception. Perhaps most importantly, increases in the numbers of subscribers connected to the network, combined with technology upgrades made possible by universal service support, benefit all users and carriers who provide services using the public switched network.

¹⁶ See USTA at 14-18.

¹⁷ Id. at 16.

(TSLRIC) of providing core universal service functions exceeds the benchmark.¹⁸ Use of such systems would, according to some proponents, eliminate the need for current pricing and support mechanisms, including the carrier common line charge, the residual interconnection charge (RIC), the Universal Service Fund (USF), long term support, etc.¹⁹

Use of uniform, comparative benchmark methodologies deserves careful study. A monthly local service rate that seems quite reasonable and “affordable” to urban customers may not be viewed as such by rural subscribers because of material differences in calling scope.²⁰ Further, as several commenters, including NECA, pointed out, basing support flows on incremental costing methods may

¹⁸ AT&T at 14-18. AT&T proposes that the Joint Board define what constitutes an “affordable rate” for consumers in all Tier 1 LEC areas. The Tier 1 LECs’ traffic-sensitive access charges set at TSLRIC should be used as benchmarks for access rates of small rural carriers located in the same region. AT&T suggests that Joint Board should presume that existing local rate for the group of core services (as augmented by an increased SLC) that recovers fully the subscriber loop portion of interstate common line is affordable for all subscribers (except those qualifying for low income assistance) and then use the weighted average of these rates (including the increased SLC) as the “nationwide affordable rate.” To the extent that the TSLRIC, as determined by a relevant cost proxy model, of providing the core set of services exceeds that level, the LEC should be able to receive national USF subsidy support for the difference between TSLRIC and the nationwide affordable rate. *Id.* at 14. Other commenters propose similar plans using TSLRIC. *See, e.g.,* MCI at 10-13 (recommends use of BCM with some modifications to determine TSLRIC; support set at amount equal to difference between TSLRIC and nationwide average rate); Teleport at 7 and 11.

¹⁹ *See, e.g.,* MCI at 6, Sprint at 20, Time Warner at 19-21. The RTC (at 17-18) points out that existing loop cost recovery mechanisms represent charges for services provided and should not entirely be considered universal service support. This suggests that, to some extent, common line and traffic sensitive costs should continue to be recovered from interexchange carriers, possibly in different forms (*e.g.,* recovery of DEM weighting requirements through a national bulk-billed charge).

²⁰ NECA 1995 NPRM Comments at 38-40. *See also* Keystone-Arthur Telephone at 8 (affordability benchmark should “reflect calling scope differences between urban and rural areas,” cites example that by using a benchmark of one-percent of national median income, benchmark would be \$28 per month and notes that in some regions of the country, “one percent of median income would be substantially lower than \$28. consideration should also be given to recognizing the proportionately higher toll volumes necessary for rural customers to obtain goods and services.”).

not be viable for all incumbent LECs.²¹ These carriers historically have been required to recover substantial plant investments using artificially long depreciation schedules. Programs that do not provide adequate means of ensuring recovery of these embedded costs for incumbent LECs would not be in compliance with the 1996 Act's requirement that support amounts be "sufficient," and may also raise questions of constitutionality.²²

Many commenters support use of various proxy methodologies to determine costs (with or without reference to affordability benchmarks).²³ Proponents of particular models, such as the Benchmark Costing Model (BCM) proposed by MCI, NYNEX, Sprint and U S WEST, recognize that proxy methods require additional study and improvement, and do not work well for small telephone companies. U S WEST, for example, states its expectation clearly that, while the proposed

²¹ See, e.g., U S WEST at 11 (payments based on model that did not include embedded costs "would not cover the full costs which LECs experience in providing basic universal service today . . . [embedded costs] reflect investments prudently made in prior years, upon which LECs are entitled to earn full recovery"); Southwestern Bell at 23-24 (under-depreciated plant exists and must be addressed). Several commenters urge the Commission to abandon mechanisms that base support on LEC revenue requirements. See, e.g., MCI at 3, MFS at 7-8, ALTS at 5-8. These commenters appear to be arguing for an end to rate of return regulation for all telephone companies, an approach that is not required by the 1996 Act and has been rejected by the Commission in the past. See, e.g., Policies and Rules for Dominant Carriers, CC Docket No. 87-313, Report and Order, 5 FCC Rcd 6786 (1990). Methods that would base universal service support payments on incentive-type plans should be applied, if at all, only to carriers operating under price cap regulation pursuant to the Commission's existing rules

²² See, e.g., RTC at 15-17 ("1996 Law codifies that universal service mechanism must support all services, must yield reasonable, affordable, and comparable rates . . . A proxy method that would limit support to some preconceived cost level based on a formula that deviates from what is needed . . . is unlawful."); United Utilities at 2 ("incumbent carriers have a right not to be subject to sudden policy changes with severe, even confiscatory, effects . . . Commission failure to provide a transition mechanism to assist small LECs under any new cost support system would represent a radical departure from past practice and raise fundamental questions of lawfulness.").

²³ See, e.g., Sprint at 9-13; Ohio PUC at 5-6.

BCM should be implemented for price cap companies as soon as possible, non-price cap LECs would remain under a funding mechanisms similar to the present USF.²⁴ NYNEX, another of the BCM's sponsors, states that the BCM should only be used to calculate support amounts for price cap LECs because:

[t]he BCM is sufficiently accurate to target support for large carriers, such as the price cap LECs, who serve wide geographic areas, because any overestimating in some areas will be offset by underestimation in other areas. However, such a model may not accurately portray the costs of a carrier that serves only a limited or a smaller area, and this could cause financial harm to small carriers. For rate of return carriers, which are typically small carriers that serve rural areas, the Commission should use actual study area costs to develop high cost assistance.²⁵

For these reasons, NECA continues to recommend that use of models such as the BCM should not be made mandatory, but that companies interested in using such models for purposes of determining costs below the study area level of detail be permitted to do so.²⁶ As the Commission moves forward with development of proxy models for these companies, however, it must assure that no harm is done to smaller companies relying on the current USF rules.²⁷ Also, the Commission

²⁴ U S WEST at 9

²⁵ NYNEX at 10-11

²⁶ A number of state regulatory commissions that otherwise support use of proxy models oppose their use for small companies. See, e.g., NYDPS at 6 (expressed concern that companies may not “fit the mold” and would either improperly receive or be denied funding); Texas PUC at 10; Wyoming PSC at 8. See also Alaska PUC at 15-16 (“BCM is not designed to work in all areas of Alaska . . . it is not evident that the annual cost factors under the [BCM] model will be appropriate for small rural local exchanges.”) There is no BCM data for Alaska at this time. Additional analysis will be needed regarding Alaska.

²⁷ See NECA 1995 NPRM Comments at 10. NECA analysis showed, for example, that application of proxy models in a “capped” fund environment could produce dramatic reductions in funding for smaller companies. Id. at 11. To avoid such results the Commission may require the fund administrator to segregate funds based on distribution mechanisms.

should recognize that application of sub-study area level costing models by large companies is likely to identify significant universal service costs that are currently masked by study area averages, and may increase the size of the fund substantially compared to the current Universal Service Fund.²⁸

Several commenters suggest that support amounts could be made “portable” among eligible carriers. In general, these commenters suggest that support amounts should be determined on a per-line basis, and paid to whichever carrier provides service.²⁹ Other commenters recognize, however, that there is not likely to be a significant number of entities qualifying for designation as “eligible” in high-cost rural areas, and accordingly suggest that different structures apply in these areas.³⁰

NECA agrees with the RTC and USTA that support amounts, if any, for non-incumbent eligible carriers serving rural areas should be based on the new carriers’ individual costs, rather than on incumbent LEC costs.³¹ Incumbent LECs have been required to make substantial plant investments in order to serve customers in high-cost areas. Support to new eligible carriers based on the embedded costs of incumbent LECs would substantially overcompensate these entities and increase the overall size of the fund unnecessarily. It would be more reasonable to require carriers that seek designation as “eligible carriers” in rural areas to obtain support, if warranted, based on their own costs. Such a requirement would not impose any undue burden on new eligible LECs. Many incumbent LECs are quite small, and are nevertheless fully subject to the Commission’s accounting

²⁸ See, e.g., NECA 1995 NPRM Comments at 11, 76-82.

²⁹ See, e.g., MCI at 5 (“provider selected by customer should be entitled to the per-line subsidy”).

³⁰ AT&T, for example, would exempt support amounts flowing to small rural telephone companies from a portability requirement. AT&T at 9, n. 12.

³¹ See USTA at 17; RTC at 11-13.

and separations rules.³² As the Ohio Consumers' Counsel states:

If new entrant LECs providing services over wire, such as cable companies, wish to become eligible telecommunications providers . . . they should be subject to the separations provisions of . . . Part 36. OCC does not necessarily endorse the entirety of the current Part 36 rules. However, until they are amended, they are the only mechanism for separating the costs of providing intrastate and interstate service, and nothing in them would confine their operation only to incumbent LECs if all carriers are to be treated equitably.³³

Actual cost data of new eligible carriers could also be compared with disaggregated incumbent LEC costs in order to develop limits on per-line support to new eligible carriers where their costs exceed those of the incumbent LEC. Such limits would be necessary in order to avoid competitive distortions and maintain reasonable fund levels.³⁴

Incumbent LECs should also be given the option to deaverage costs below the study area level of detail for purposes of determining support. As NECA pointed out in its comments (at 9-10), this step would be necessary because some study areas have high average costs, but contain areas (such as towns or cities) that are lower-cost. Payments or transfers of support amounts to non-incumbent eligible carriers based on the study area averages of incumbent carriers would tend to overcompensate non-incumbent carriers that concentrate marketing efforts on low-cost or high-volume segments of

³² Park Region at 3 ("numerous very small local exchange carriers of less than 100 lines comply with the cost separation accounting rules")

³³ Ohio Consumers' Counsel at 3. NECA pointed out in its comments (at 9-10) that the Commission's cost accounting rules have been used for many years by incumbent LECs, many of which are quite small, and that application of these rules to new eligible carriers would not appear to impose any undue burdens

³⁴ See USTA at 17 (in no case should payments to a new carrier exceed the incumbent exchange carrier's support per line.); NECA at 8-11.

a given service area.³⁵ Further, support should be provided only to the extent that carriers actually assume the risks of providing high-cost facilities.³⁶

The record does not support the use of competitive bidding to establish support amounts. Several parties express concern that these mechanisms would have adverse effects on service quality,³⁷ would be impractical,³⁸ and would be potentially inconsistent with the 1996 Act.³⁹ NECA agrees that the Commission should not pursue this option

Finally, in the event that the Commission chooses to change or reduce current levels of support (in spite of the record evidence to the contrary), reasonable transition mechanisms must be

³⁵ NECA suggested in its comments (at 10) that it would be possible to develop engineering models that could be used by incumbent LECs to disaggregate the results of current cost studies to smaller geographic zones for comparison purposes. The availability of disaggregated costs for incumbent LECs could aid regulators in determining support levels for any new eligible carriers that may be designated, and could also enable regulators to determine resale prices for incumbent LEC facilities with greater accuracy. See also RTC at 11-13

³⁶ As the RTC points out (at 9), local service rates for rural telephone companies typically cover only a portion of the LEC's costs. In cases where incumbent LECs are required to provide interconnection to resale carriers at below-cost rates, it would make no sense to pay support amounts to the resale carrier, who has already received the benefit of support amounts reflected in discounted rates for the resold service

³⁷ See, e.g., NYNEX at 10, n. 15 (“[s]uch a system would be difficult to administer, and it would not necessarily represent a better method of identifying high cost areas. It would also create large variations in the amount of support that is directed at each high-cost area based on the level of competition and the business objectives of the bidders.”). See also NECA at 11 and n. 20 (competitive bidding processes might result in a “race for the bottom” and might not protect against service discontinuance).

³⁸ For example, the RTC (at 17) points out that bidding processes might involve the Commission in regulatory review of construction plans on an initial and continuing basis. USTA (at 19-20) supports use of voluntary bidding mechanisms only for areas that no carriers are otherwise willing to provide service

³⁹ See, e.g., United Utilities at 2

put in place to permit carriers to adapt.⁴⁰ Companies that have made significant investments in serving high-cost areas in reliance on the current cost recovery rules, especially, need time to adapt.⁴¹ Transition periods should be proportional to the magnitude of cost shifts. A major change in the USF rules, for example, should be phased in over an extended period of time, similar to the eight years for the SPF phase-down.⁴²

II. THE COMMISSION SHOULD REPLACE THE CURRENT TARIFF-BASED UNIVERSAL SERVICE COLLECTION MECHANISM WITH A REVENUE-BASED CONTRIBUTION SYSTEM.

The record supports replacement of the current PSL-based universal service contribution methodology with a revenue-based system applicable to all interstate carriers and service providers. Many parties point out that the 1996 Act requires contributions to the new universal service support mechanism to be made on an equitable and nondiscriminatory basis by all interstate telecommunications carriers, and potentially other providers, and that a revenue-based system would

⁴⁰ Other parties support reasonable transition periods. USTA, for example, argues (at 18) for a four-year transition period during which EUCL charges would be rebalanced, CCL charges and LTS reduced for all carriers, and USF and weighted DEM frozen for non-rural carriers. See also Florida PSC at 12 (believes Act “permits any actions in the proceeding that affects recipients of existing funding to be phased in over at transitional period;” proposes three to five-year phase-in); Mo PSC at 8 (proposes five-year transition); United Utilities at 1-2 and Alaska Tel. Assoc. at 4 (both suggest ten-year transition)

⁴¹ Lenders such as the Rural Utilities Service (formerly, the REA) typically amortize loans over a lengthy period. Possible abrupt changes to universal service funding mechanisms injects uncertainty into the process, unnecessarily increasing risk and capital costs.

⁴² Calculation of a reasonable time for transition would depend, of course, on the extent of any impacts. As noted above, NECA looks forward to analyzing any specific proposals advanced by the Commission and/or the Joint Board in terms of likely effects and corresponding transition requirements.

fulfill this requirement.⁴³

NECA pointed out in its comments that it has successfully administered the interstate TRS fund using an interstate revenue-based contribution methodology applicable to all interstate common carriers since 1993. Based on this experience, NECA stated that it could administer a universal service support system based on interstate revenues in compliance with the 1996 Act.⁴⁴ Similar to TRS, the administrator could be directed to file data with the Commission establishing fund revenue requirements. After opportunity for comment, the Commission could approve proposed fund levels and prescribe payment formulas and procedures.⁴⁵ As in the case of TRS, these procedures could include a flat minimum amount for providers with revenues below a certain threshold.⁴⁶ This would

⁴³ The Wyoming PSC suggests (at 4) that “it would be more properly comparable and much fairer to base the assessment on gross retail revenues.” A number of other commenters also argue for the use of retail revenues as an allocator. See, e.g., AT&T at 8; Cincinnati Bell at 15; 360° Communications at 9. Other parties argue for the use of a net revenue allocator. See e.g., ALTS at 18; MCI at 15-16; NCTA at 24; Telecommunications Resellers Assoc. at 8. U S WEST argues (at 16-19), however, that the latter approach (revenues net of payments to other carriers) shifts a disproportionate share of the universal service burden to exchange carriers and would not be competitively-neutral. Similarly, the Wyoming PSC states (at 4) that if netting approach is used “a disproportionate burden would fall on those providing the service at wholesale; and an inaccurate picture of the value of the system to the reseller would be administratively generated.”

⁴⁴ As NECA explained in its 1995 NPRM Comments, allocation methodologies that rely on minutes of use or lines may not be as equitable or competitively-neutral as revenue-based methodologies. The Commission reached a similar conclusion in its 1995 Regulatory Fees Order. See Assessment and Collection of Regulatory Fees for Fiscal Year 1995, Price Cap Treatment of Regulatory Fees Imposed by Section 9 of the Act, Report and Order, 10 FCC Rcd 13512, ¶ 134 (1995). NECA does not recommend adoption of non-revenue alternatives.

⁴⁵ Commission rules should expressly require carriers to pay their universal service bills, as is the case today for TRS contributors 47 C F R § 64.604. This would greatly facilitate the collection of funds.

⁴⁶ Under current TRS procedures, all interstate carriers with revenues of less than \$300,000 in annual revenue are required to pay \$100 and all other carriers contribute to the TRS fund based on a percentage of their gross interstate revenue.

alleviate concerns about the administrative problems of calculating and collecting de minimis support payment amounts.

A revenue-based collection mechanism could also be used to fund programs mandated by section 254(h) of the Act (i.e., discounted services to rural health care providers, educational institutions and libraries), as well as any additional programs authorized for low-income consumers. As NECA suggested in its Comments, policy decisions to support additional services and/or discounts, as required by the 1996 Act, can be accomplished by using existing Lifeline Assistance rules as a model.⁴⁷ The proposed use of discount mechanisms for rural health care providers, educational institutions and libraries, for example, appears to parallel existing mechanisms for low income subscribers, in that qualified individuals or entities (as defined in the 1996 Act and Commission rules) would receive service at a rate that is less than that charged to other subscribers.

Comments filed in this proceeding highlight the need for such programs, but also illustrate their complexity.⁴⁸ NECA agrees that policy decisions in these areas should be considered carefully, and should include consideration of administrative feasibility. In particular, it may be difficult to *determine the nature of services provided, and the amount of claimed differences between normal and discounted rates.* Carrier-provided certifications may be useful in supporting reimbursement claims. At a minimum, carriers claiming reimbursement must be required to maintain adequate documentation

⁴⁷ For example, if a decision is made to make discounts available for non-conventional residential services, rules similar to those governing the calculation of Lifeline Assistance revenue requirements could be implemented that would require carriers to document and submit allowable discount claims to the fund administrator for reimbursement.

⁴⁸ USTA (at 6-9), for example, points out that multiple layers of governmental authorities as well as different types of providers may be involved in provisioning service to educational institutions, and that many discreet components need to be addressed

of rates and costs, and all claims must be subject to audit by the administrator and/or the Commission. Finally, in establishing a new funding program for service discounts to rural health care providers, educational institutions and libraries, the Commission must assure that no adverse impacts occur with respect to other universal service programs.⁴⁹

III. THE COMMISSION SHOULD APPOINT NECA AS ADMINISTRATOR OF THE NEW UNIVERSAL SERVICE FUND.

The record supports the use of a private entity, specifically NECA, to administer federal universal service support mechanisms. Numerous parties describe the value of NECA's expertise and the scope of NECA's in-place resources.⁵⁰ These commenters believe that the Commission should continue to rely on NECA as administrator, rather than delegate the function to separate state administrations or to start over with a new entity.⁵¹

The Wyoming PSC states that "[f]or the federal universal service fund, it would be wise to

⁴⁹ See *supra* n. 27 and accompanying text. In this regard, some commenters suggest establishment of a separate or segregated fund for services discounts. See, e.g., USTA at 6-12; RTC at 18-19; Alaska Tel. Assoc. at 8; Oregon and Washington Tel. Assoc. at 17. Similar to current Universal Service and Lifeline Assistance programs, funds could be collected on a consolidated basis but remain separately identified.

⁵⁰ See, e.g., Frederick & Warinner at 4 (NECA is currently in place; is staffed with industry professionals; and "possesses the body of knowledge and experience necessary to implement the results of this proceeding efficiently and effectively")

⁵¹ In general, parties opposing delegation of administrative functions to individual state agencies express concerns about inefficiencies and possible inconsistencies between states and the unnecessary addition of complexity to the process. See, e.g., Oregon and Washington Indep. Tel. Assoc. at 16-17 ("continued use of NECA as an administrator would be far more efficient than establishing a new non-governmental administrator and clearly more efficient than creating a government bureaucracy to serve as administrator"); Idaho PUC at 17-18. See also Missouri PSC at 21 ("[t]he USF, as a national program, benefits from having one national administrator. For that reason, the MoPSC opposes delegating the fund's administration to the States.")

have a single administration and distribution mechanism” and suggests NECA because “it has an important base of knowledge and experience in analogous matters as well as a history of providing stable, reliable and accurate service to the industry.”⁵² The Indiana URC staff supports administration of the fund by a neutral third party, “but does not believe the wheel has to be reinvented in order to ensure that universal service mechanisms are administered fairly, consistently and efficiently ”⁵³

Indiana goes on to state that,

[a]s administrator of the existing Universal Service Fund, the National Exchange Carrier Association (NECA) has demonstrated its proficiency in meeting the conditions specified in the Notice. The 1996 Act requires changes in the structure of the Universal Service Fund and its funding that the IURC Staff believes will best be accomplished administratively by using the current administrator - NECA.⁵⁴

The Idaho PSC, North Dakota PSC,⁵⁵ Pennsylvania PUC ⁵⁶ and the South Carolina PSC⁵⁷ all

⁵² Wyoming PSC at 5.

⁵³ Indiana URC at 5

⁵⁴ Id. at 5-6. See also ICORE at 19 (“Since NECA already administers the tariff and revenue distribution processes for many small LECs, as well as industry-wide USF, Lifeline Assistance, Link-Up America and TRS programs, it would seem to be the logical administrator of any enhanced or new universal support mechanisms.”).

⁵⁵ North Dakota PSC at 4. (“[w]e believe that the National Exchange Carrier Association has done an excellent job of administering the current Universal Service Fund and should serve as administrator of the ‘new’ universal service fund ”)

⁵⁶ Pennsylvania PUC at 25 (“given the requirements of the 1996 Act for separate and distinct universal service support mechanisms at the state and federal levels and the ‘large-scale information processing and data base capabilities’ that will be necessary to manage the fund, we believe that the FCC should designate a third party administrator for federal fund administration. We believe that NECA has done an excellent job of administering the fund in the past and we would support their continued oversight and administration of the federal fund in the future.”)

⁵⁷ South Carolina PSC at 2 (NECA should continue to administer the interstate fund).

endorse NECA's continuation as administrator of the Universal Service Fund.⁵⁸ The Idaho PSC states that, "[w]hile some would argue that competition and bidding should be applied also to the choice of support administrator in the hopes of finding an organization to do it better (cheaper), NECA's historical understanding and backlog of expertise in this endeavor puts its high on a learning curve others would have to climb from the bottom."⁵⁹

The Colorado Indep. Tel. Assoc. states that it "strongly [favors] continuing with a winner as far as the agent for administration of the new generation universal service supports. The National Exchange Carrier Association has the professional know-how, the tools, the non-profit approach and a sterling reputation which makes it, in our opinion, a natural for administration of the universal service mechanisms in the future."⁶⁰

NECA currently collects TRS fund amounts from approximately 3,000 interstate carriers, and processes complex universal service, lifeline assistance and pooling data from over 1,200 LEC study areas. Its data processing resources include a settlements system that routinely handles over 170,000 data transactions per month. It has created and maintained extensive verification programs that permit

⁵⁸ The Maine Public Utilities Commission, Montana Public Utilities Commission, Nebraska Public Service Commission, New Hampshire Public Utilities Commission, New Mexico State Corporation Commission, Utah Public Service Commission, Vermont Department of Public Service and Public Service Board and Public Service Commission of West Virginia in their Joint Comments (at 22-23) state that Vermont "has had a neutral fund administrator since 1994 for its Universal Service Fund . . . The Vermont system, as administered by NECA, has been working well, and may be an adequate administrative model for a federal program."

⁵⁹ Idaho PUC at 7.

⁶⁰ Colorado Indep. Tel. Assoc. at 2. The FCC should appoint NECA since it is "already fully equipped to handle the new universal service support mechanisms collection and distribution duties." Id. at 7.

various historical comparisons, “reasonableness” checks, and statistical analyses of these data.⁶¹ In its role as administrator of the TRS fund, NECA has shown that it can collect and analyze cost data from a variety of entities including exchange carriers, interexchange carriers, state agencies and other providers. NECA is able to perform on-site reviews of provider data as needed, and its processes have been subjected to rigorous internal and external audits with no major or significant findings. NECA clearly has the capability to administer new federal universal service mechanisms.⁶²

NECA further explained in its Comments that it is a non-profit organization, established pursuant to the Commission’s rules, specifically for the purposes of administering interstate access charge tariffs, associated revenue pools, and the Commission’s universal service programs, and is therefore uniquely able to respond to Commission direction and needs. NECA has compiled an excellent track record of efficiency and continual improvement in its operations, with constant dollar reductions in administrative expenses shown in each year of its operations.⁶³

Several commenters nevertheless assert that new federal universal service administrative

⁶¹ NECA cost study verification procedures are described in detail in NECA’s Comments filed on April 14, 1993 in the Safeguards to Improve the Administration of the Interstate Access Tariff and Revenue Distribution Processes, Notice of Proposed Rulemaking, 8 FCC Rcd 1503 (1993) (NECA Safeguards Proceeding). See also NECA 1994 NOI Reply at 36-37.

⁶² See Iowa Utilities Board at 6-7 (“(NECA) has developed, managed and administered the current USF funding mechanism since its inception in 1984. During NECA’s administration of the current program, the organization has developed extensive internal systems, procedures and controls to insure the integrity of data collections, calculations, and collection and distribution of funds. It is very apparent that NECA has a proven track record in the management of data collections, fund and/or pooling administration in an environment containing specific rules and responsibilities. NECA has also demonstrated its ability to develop and manage large-scale information and data base systems.”)

⁶³ Keystone-Arthur Tel. at 2 (“[t]he existing interstate administration provided by . . . (NECA) . . . could provide the most cost-effective fund administration on a going-forward basis.”)

functions should be assigned to some other entity that is unaffiliated with any industry segment.⁶⁴ These parties typically assert that a non-affiliated administrator is needed to assure fairness in collections and distribution processes.⁶⁵ NECA believes, however, that the best way to assure that universal service funds are administered in an even-handed and fair manner is to appoint an administrator that has substantial experience with, and in-depth knowledge of, the telecommunications industry and the Commission's rules.⁶⁶ As the RTC points out, administration of a new fund "will require a mixture of expertise in the minutiae of communications industry structure, cost characteristics, accounting practices, and an understanding and commitment to the universal service goals of the Act. . . . NECA is uniquely positioned in the industry to broaden its capability to meet the requirements of the new USF effectively, efficiently, and with minimal

⁶⁴ See, e.g., Ameritech at 24 (suggests a large accounting firm); LCI at 6.

⁶⁵ See, e.g., NCTA at 25. The 1996 Act includes no such requirement. In fact, the final version S. 652 deleted a provision contained in the earlier version of the Senate Bill that called for "an independent, non-governmental entity or entities" to administer the fund. Even if it had been included in the 1996 Act, this language would not have precluded NECA from administering a new universal service mechanism. It is worth noting that similar concerns about NECA's supposed lack of neutrality were raised in the context of CC Docket No. 90-571 (the Commission's TRS proceeding). Yet, NECA has received considerable praise, and no complaints, for its work in administering the TRS program, and was recently reappointed by the Commission to a four-year term. See NECA at 22-23. It should also be noted that NECA has successfully served as neutral administrator of the Vermont USF program since 1994, with no party alleging bias.

⁶⁶ See Minn. Indep. Coalition at 23 (NECA has a demonstrated ability to administer similar funding mechanisms and has in place the organization needed to do so). See also New Hope Tel. Coop. at 5, Ardmore Tel. Coop. at 5.